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SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1949

No. 116.

BENNETT I. FIELDING and FRANCES BARRETTA, suing on behalf of themselves and all other stockholders of OGDEN CORPORATION who may join in and contribute to the expenses of this action, for and on behalf of OGDEN CORPORATION,

Respondents,

EDWARD A. MILLER and MARY MILLER,

Respondents-Intervenors,

IRVING W. MENCHER,

Respondent-Intervenor,

against

OGDEN CORPORATION,

Petitioner,

and

CHARLES ALLEN, JR., RITA ALLEN, HAROLD ALLEN and SAMUEL ELGORT, individually and as co-partners doing business under the firm name and style of ALLEN AND COMPANY, JACOB L. HOLTZMANN, LILLIAN HOLTZMANN, BENJAMIN H. BREWSTER, LEON COLE, L. BOYD HATCH, MAURICE L. SINDEBAND, LILLIAN SINDEBAND, HOWARD L. FOGG, RALPH B. DURELL, Executor of the Last Will and Testament of Thomas P. Durell, deceased,

Defendants,

and

HELEN S. FOGG and C. W. RETNAUER,

Defendants.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT AND BRIEF IN SUPPORT THEREOF

RICHARD JOYCE SMITH,
Counsel for Petitioner.

HENRY S. REEDER,
BERNARD L. SANOFF,
Of Counsel.

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Supreme Court of the United States

OCTOBER TERM, 1949

No. .

BENNETT I. FIELDING and FRANCES BARRETTA, suing on behalf of themselves and all other stockholders of OGDEN CORPORATION who may join in and contribute to the expenses of this action, for and on behalf of OGDEN CORPORATION,
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CHARLES ALLEN, JR., RITA ALLEN, HAROLD ALLEN and SAMUEL ELGORT, individually and as co-partners doing business under the firm name and style of ALLEN AND COMPANY, JACOB L. HOLTZMANN, LILLIAN HOLTZMANN, BENJAMIN H. BREWSTER, LEON COLE, L. BOYD HATCH, MAURICE L. SINDEBAND, LILLIAN SINDEBAND, HOWARD L. FOGG, RALPH B. DURELL, Executor of the Last Will and Testament of Thomas P. Durell, deceased,
Defendants,

and

HELEN S. FOGG and C. W. RETNAUER,
Defendants.

PETITION

TO THE HONORABLE CHIEF JUSTICE OF THE UNITED STATES AND THE HONORABLE ASSOCIATE JUSTICES OF THE SUPREME COURT OF THE UNITED STATES:

The petitioner, OGDEN CORPORATION (herein sometimes referred to as "Ogden"), respectfully prays that a writ

of certiorari issue to review the Order of the United States Court of Appeals for the Second Circuit, filed April 12, 1950 (R. 129), which reversed an Order of the United States District Court for the Southern District of New York entered October 3, 1949 (R. 111-113), granting the petitioner security for costs in the sum of $12,500, pursuant to Section 61-b of the New York General Corporation Law, and reversed and remanded the case for proceedings not inconsistent with the opinion of the Court.*

The opinion of the Court of Appeals for reversal (per L. Hand, Swan and Chase, Circuit Judges) is at R. 120-128, and the opinion of the District Court (per Ryan, J.) is at R. 99-110.

Jurisdiction

The jurisdiction of this Court is invoked under 28 U. S. C. § 1254(1) and § 2101(C). The Order of the Circuit Court of Appeals, reversing the judgment of the District Court, was filed April 12, 1950.

Statutes Involved

The statutes involved are the Rules of Decision Act (28 U. S. C. § 1652) and Section 61-b of the New York General Corporation Law (Laws of New York 1944, Chap. 668, as amended by Laws of New York 1945, Chap. 869).

The Rules of Decision Act provides as follows:

> "The laws of the several states, except where the Constitution or treaties of the United States or Acts of Congress otherwise require or provide, shall be regarded as rules of decision in civil actions in the courts of the United States, in cases where they apply. June 25, 1948, c. 646, 62 Stat. 944."

Section 61-b of the New York General Corporation Law provides as follows:

> "§ 61-b. *Security for expenses.*—In any action instituted or maintained in the right of any foreign

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* References to record are to page numbers.

or domestic corporation by the holder or holders of less than five per centum of the outstanding shares of any class of such corporation's stock or voting trust certificates, unless the shares or voting trust certificates held by such holder or holders have a market value in excess of fifty thousand dollars, the corporation in whose right such action is brought shall be entitled at any stage of the proceedings before final judgment to require the plaintiff or plaintiffs to give security for the reasonable expenses, including attorney's fees, which may be incurred by it in connection with such action and by the other parties defendant in connection therewith for which it may become subject pursuant to section sixty-four of this chapter, to which the corporation shall have recourse in such amount as the court having jurisdiction shall determine upon the termination of such action. The amount of such security may thereafter from time to time be increased or decreased in the discretion of the court having jurisdiction of such action upon showing that the security provided has or may become inadequate or is excessive. * * *"

Summary Statement of Matter Involved

The question involved is whether, under the Rules of Decision Act, Section 61-b of the New York General Corporation Law is applicable to this stockholders' derivative action, instituted in the federal court for the Southern District of New York, so as to require the respondents to give Ogden Corporation, in whose right the action is brought, security for the reasonable expenses, including attorney's fees, which may be incurred by it in connection with the action or for which it may become subject under Section 64 of the New York General Corporation Law.*

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* In this connection it should be noted that the same corporate transactions herein questioned were the subject of a similar action brought in the New York Supreme Court, in which the plaintiffs were represented by the same firm of attorneys as the respondents in the case at bar. The State court action was dismissed because the plaintiffs failed to furnish security for expenses, initially fixed at $6,000 (*Malkan & Mencher* v. *Charles Allen et al.*, N. Y. L. J., April 22, 1949, page 1450; id., October 14, 1949, page 839).

The complaint purports to set forth two causes of action, in each of which directors and officers of Ogden, or their legal representatives, are named as defendants and are charged with a breach of their fiduciary duties. Other persons, with whom the officers and directors of Ogden are alleged to have conspired in carrying out the transactions complained of, are also named as defendants.

Under Section 64 of the New York General Corporation Law, the directors and officers of Ogden who are parties to the action would be entitled to have Ogden reimburse them for reasonable litigation expenses, including attorney's fees, actually and necessarily incurred by them in connection with the defense of the action, except in so far as such directors and officers may be adjudged liable for negligence or misconduct in the performance of their duties. A similar indemnification provision is contained in Section 16-A of the By-Laws of Ogden adopted pursuant to Section 2(10) of the Delaware Corporation Law (R. 63-64).*

To protect itself against liability for such expenses, Ogden moved in the District Court for security. That Court, following the decision of this Court in *Cohen* v. *Beneficial Industrial Loan Corporation*, 337 U. S. 541 (1949), granted Ogden security in the amount of $12,500 (R. 110). The *Cohen* case held that a New Jersey statute, similar in all material respects to Section 61-b of the New

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* No question is presented as to the applicability of Section 61-b of the New York General Corporation Law by its terms. The plaintiffs own in the aggregate 755 out of 3,403,661 shares outstanding of Ogden, representing less than .0023% of the outstanding shares, having a market value of less than $1,500 (R. 80). The defendants Brewster, Cole, Hatch and Sindeband were directors of Ogden and the defendant Fogg (since deceased) was an officer of Ogden, at the time when the challenged transactions occurred. These defendants, together with the defendant Ralph B. Durell, Executor of the Last Will and Testament of Thomas P. Durell, deceased, also a director of Ogden at the time these transactions occurred, have all been served in the action and have appeared by three separate firms of attorneys (R. 80).

York General Corporation Law, applied in the federal courts.

The Court of Appeals recognized the controlling effect of the decision in the *Cohen* case as to the first cause of action pleaded in the complaint at bar, in which jurisdiction of the federal court is predicated upon diversity of citizenship. However, it denied the applicability of the decision in the *Cohen* case to the second cause of action, although jurisdiction of the federal court as to this cause is also expressly predicated upon diversity of citizenship. In so doing, the Court of Appeals held that, in the second cause of action, the respondents had asserted a claim "based on a law of the United States", i.e., the Transportation Act (R. 124), that the allegations predicating jurisdiction of the federal court upon diversity of citizenship were "a defect in pleading which may be disregarded as surplusage" (R. 124), and that the respondents should not have been required "to furnish security under section 61-b as a condition precedent to the prosecution of their second cause of action" (R. 127).

The Complaint

Although the issue as to the applicability of Section 61-b of the New York General Corporation Law is limited by the decision of the Court below to the second cause of action, consideration will need to be given to the allegations of the first cause of action, consisting of some twenty-three numbered paragraphs, all but two of which paragraphs (pars. 14 and 15) and a subdivision of another paragraph (par. 17(a)) are realleged as integral parts of the second cause of action (R. 20, 21).

First Cause of Action

The transaction complained of in the first cause of action is the sale by Ogden in December, 1945, of its interests in the Litchfield and Madison Railway Company (Litchfield)

and Mt. Olive and Staunton Coal Company (Mt. Olive) to the defendant Holtzmann. It is alleged in the complaint that the officers and directors of Ogden and the defendants Holtzmann and Allen & Company arranged this sale for a grossly inadequate price pursuant to "a scheme, plan and conspiracy wrongfully, fraudulently and unlawfully to divest Ogden of its assets and properties" (R. 13).

It is alleged that in carrying out this plan Ogden was caused to sell to the defendant Holtzmann for $1,758,883.33 its interests in Litchfield and Mt. Olive, which interests "were of the real and actual value of at least $7,625,000" (R. 13), that in acquiring such interests Holtzmann was "acting as the agent, dummy and instrumentality" of Allen & Company, and that the sale was made to Holtzmann "for the deliberate purpose and design, amongst others, of avoiding the submission of said transaction to the Interstate Commerce Commission for its approval" (R. 14). It is then further alleged that the "consideration paid to Ogden" was "grossly inadequate" (R. 14), that after the sale to Holtzmann, Holtzmann "on behalf of Allen & Company" transferred certain of the shares of stock of Litchfield and Mt. Olive to Fogg, an officer of Ogden, and his wife, and to Sindeband, a director of Ogden, and his wife (R. 14-15), and generally that in causing Ogden to dispose of its interests in Litchfield and Mt. Olive "the defendant directors and officers of Ogden acted with reckless and complete indifference to the interests and welfare of Ogden" (R. 16).

Federal jurisdiction over this cause of action is predicated upon diversity of citizenship (R. 19).

Second Cause of Action

A reading of the second cause of action reveals at once its essential identity with the first. *Every allegation of breach of fiduciary duty set forth in the first cause of action*

is realleged as part of the second cause of action. As the District Court stated (R. 105):

> "Insofar as the pleading of the second count there is no real difference in either complaint. Fraud, inadequacy of consideration for transfer of assets of Ogden and the despoilment of Ogden to the benefit of defendants are the gravamen of both counts of each complaint."

The second cause of action, however, is directed more particularly to the sale by Ogden of its interests in Litchfield. After realleging *in toto* the allegations of the first cause of action to the effect that the defendants breached their fiduciary duties in making this sale (R. 44), it is alleged additionally as an incident of the asserted breach of fiduciary duty that the sale of Litchfield violated Section 5 of the Transportation Act (R. 44-45). The respondents' contention in this respect is that the sale to Holtzmann, acting as an alleged agent for Allen & Company, was "indirectly" a sale to Allen & Company, which, then being in control of another carrier, would have been required under Section 5 of the Interstate Commerce Act to obtain the prior approval of the Interstate Commerce Commission for the acquisition of Litchfield (R. 44).

The relief requested, as to both causes of action, is that the defendants reconvey to Ogden all of the assets alleged to have been wrongfully transferred and that they account to Ogden for such assets and the profits received thereon (R. 46).

Federal jurisdiction over the second cause of action purports to be predicated upon the alleged violation of a federal statute as well as upon diversity of citizenship. As to this cause of action, the jurisdictional allegations are as follows (R. 45-46):

> "37. This action arises under the laws of the United States, including Transportation Act of 1920 (41 Stat. 474), as amended by the Act of June 16,

1933 (48 Stat. 211) and the Act of September 18, 1940 (54 Stat. 905), U. S. C. Title 49, Sec. 1, et seq., as hereinabove more fully appears, and jurisdiction of this court depends thereon, as well as on diversity of citizenship."

Questions Presented

In holding that the respondents should not be required to give security as a condition precedent to the prosecution of their second cause of action, the Court of Appeals recognized that, in view of this Court's ruling in the *Cohen* case, its decision was "not free from doubt". We submit that the decision below raises important questions which should be reviewed by this Court, viz.:

1. Whether the plaintiffs in a derivative stockholders' suit in the federal courts may circumvent the State security requirements by adding to the essential averments of a cause of action for breach of fiduciary duty an allegation that one of the successive steps incidentally violated a federal statute.

2. Whether, in the absence of other controlling federal statutes, the decision of this Court in the *Cohen* case requiring the giving of security is limited to stockholders' derivative actions where federal jurisdiction is predicated *solely* upon diversity of citizenship.

Reasons Relied On for the Allowance of the Writ

1. In holding that the second cause of action in the complaint states a claim that "arises under" the laws of the United States (i.e., Section 5 of the Transportation Act), the decision of the Court below is in conflict with the decisions of this Court and with the decisions of other federal courts. In effect, the Court below has held that by the inclusion in a complaint of non-essential allegations of an alleged violation of a federal statute, the pleader may

transform an action over which a federal court would have no jurisdiction, absent diversity of citizenship, into one federal in nature as to which a State requirement for security is not applicable. Such a holding is in conflict with the principle enunciated in *Gully* v. *First National Bank in Meridian*, 299 U. S. 109 (1936), that for a case to arise under the Constitution or laws of the United States the federal claim relied on "must be an element, and an essential one, of the plaintiff's cause of action" (299 U. S. at p. 112). The decision below would permit litigants in stockholders' derivative suits as well as other types of actions, essentially local in nature, to invoke the jurisdiction of the federal courts upon mere sham or frivolous allegations, non-essential to the basic claims asserted, that some federal statute had also been violated.

2. In holding that the respondents should not be required to post security as a condition of prosecuting their second cause of action, the Court below has failed to give effect to a State-declared policy of requiring security in stockholders' derivative actions which this Court held in the *Cohen* case, *supra*, was to be given effect in the federal courts, and its decision is contrary to, or at least materially qualifies, the decision of this Court in that case. In the *Cohen* case, this Court recognized that the State security requirement was "substantive" in nature (327 U. S. at p. 555). Notwithstanding the holding of this Court, the Court below held in effect that, even in the absence of a controlling federal statute, security should be given or denied in accordance with whether a non-federal or possible federal claim is asserted, and that, even if a non-essential federal claim is asserted, security should be denied as to all claims. The importance of the question to litigants in the federal courts as to whether a federal court should apply a State security statute was recognized by this Court when it granted certiorari in the *Cohen* case (336 U. S. 917). The decision of the Court below, the correctness of which that Court itself admitted "was not free from doubt" (R.

127), if not in conflict with this Court's decision in the *Cohen* case, has placed important limitations upon it and should be reviewed.

WHEREFORE, your petitioner respectfully prays that a Writ of Certiorari be issued out of and under the seal of this Honorable Court, directed to the Court of Appeals for the Second Circuit, commanding that Court to certify and send to this Court for its review and determination, on a day certain to be therein named, a full and complete transcript of the record and of all proceedings in the case numbered on its Docket No. 21567, and entitled as above shown; and that the Order of that Court, filed April 12, 1950, be reversed; and that your petitioner may have such other and further relief in the premises as to this Honorable Court may seem just and proper.

Dated: New York, N. Y.
June 7, 1950.

RICHARD JOYCE SMITH,

RICHARD JOYCE SMITH,
Counsel for Petitioner.

HENRY S. REEDER,
BERNARD L. SANOFF,
of Counsel.

ARGUMENT

POINT I

The decision of the Court below is in apparent conflict with the principles enunciated by this Court in *Gully* v. *First National Bank in Meridian*, 299 U. S. 109.

In reaching its decision the Court below invoked the principle first enunciated in *The Fair* v. *Kohler Die & Specialty Co.*, 228 U. S. 22, 25 (1913), and more recently stated in *Bell* v. *Hood*, 327 U. S. 678, 681 (1946), that the party who brings a suit "is master to decide what law he will rely upon". Neither decision, however, was even remotely related to the question of the extent to which a federal court should follow the policy of State law. Moreover, in resorting to a claimed analogy of such decisions the Court below ignored the essential nature of the second cause of action as one to enforce an accounting by corporate officers and directors for alleged breaches of their common law fiduciary duties in which a claimed violation of a federal statute is not "an element, and an essential one" of the cause of action pleaded (*Gully* v. *First National Bank in Meridian*, 299 U. S. 109, 112 [1936]; see pp. 14-18, *post*).

In the *Fair* case, the question was whether a federal court had jurisdiction of an action under the patent law. In holding that the federal court did have jurisdiction, the Court said (228 U. S. at p. 24):

> "Obviously the plaintiff sued upon the patent law, so far as the purport and intent of the bill is concerned. *It was a resident of the same State as the defendant and could have had no other ground.* In the earlier paragraphs of the bill it charged an infringement of its patent rights in general terms,

> and it sought triple damages, which it could have done only by virtue of the statute. * * *" [Italics supplied]

In the *Bell* case, the question was whether a federal court had jurisdiction of an action seeking recovery "squarely on the ground that respondents violated the Fourth and Fifth Amendments" (327 U. S. at p. 681). In holding that the Court did have jurisdiction of such an action, this Court noted that the alleged violations of the Constitution formed "the sole basis of the relief sought" (327 U. S. at p. 683).

In whatever manner the respondents' second cause of action may be described, it is clearly not one where the alleged violation of a federal statute furnishes "the sole basis" of the relief sought, and moreover the respondents were careful not to make it such. This is abundantly clear from the fact that they have realleged in the second cause of action all of the essential allegations of breach of fiduciary duty contained in their first cause of action, and have named as defendants all the defendants named in the first cause of action. In addition, and by their own allegations, they have invoked the jurisdiction of the federal court over both causes of action upon the grounds of diversity of citizenship.

The Court below correctly recognized that the essential nature of the first cause of action was one charging corporate officers and directors "with conspiracy, fraud, and breach of fiduciary duties" (R. 121). This Court has many times recognized that such actions are dependent upon State law and are subject to plenary regulation by the State. It was upon this theory that the Court in *Cohen* v. *Beneficial Industrial Loan Corporation,* 337 U. S. 541 (1949), held that a New Jersey security statute similar in all respects to Section 61-b of the New York General Corporation Law should be applied in federal courts sitting in New Jersey.

Despite the fact that all the allegations of "conspiracy, fraud and breach of fiduciary duties" are realleged as the gravamen of the second cause of action, the Court below has held that because of the addition of an allegation that the defendants in committing breaches of fiduciary duty incidentally also violated a federal statute, respondents have stated a claim based upon a federal statute. The Court of Appeals held, furthermore, that the right to sue on such a claim is "federally conferred" and hence should not be subject to State requirements for the giving of security (R. 126).

The claimed violation of the Transportation Act, however, is not an "essential element" of the cause of action asserted for breach of fiduciary duty; and the right to maintain suit thereon is not "federally conferred".* Under their general equitable jurisdiction, the federal courts have from time immemorial entertained stockholders' derivative actions, just as they have entertained on the law side actions on contract and in tort, but, in the absence of a controlling federal statute, it is a misnomer to describe the right to maintain such actions as "federally conferred". Such right, as this Court so clearly stated in the *Cohen* case, is "dependent upon state law" and is subject to "most complete and penetrating regulation" by the State (337 U. S. at p. 549).

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* The Transportation Act does not confer upon stockholders the right to sue, and fails to provide for a private right of action in the corporation itself. No case is found in which the Courts have sustained a private right of action, on behalf of a corporation, for an alleged violation of Section 5 of the Act. Under analogous statutes, the existence of such a right has been specifically denied. (See *Steckler* v. *Pennroad Corporation*, 44 F. Supp. 800, aff'd 136 F. 2d 197 [3rd Cir. 1943], cert. den. 320 U. S. 757 [1945]; *Nelson* v. *Leighton*, 82 F. Supp. 661 [D. C. N. D. N. Y. 1949].)

The alleged federal claim fails to meet the tests established in *Gully* v. *First National Bank.*

In *Gully* v. *First National Bank in Meridian,* 299 U. S. 109, this Court reviewed the "well established" tests to be applied in determining when a case arises under the Constitution or laws of the United States, as follows (299 U. S. 109, at p. 112):

> "How and when a case arises 'under the Constitution or laws of the United States' has been much considered in the books. Some tests are well established. To bring a case within the statute, a right or immunity created by the Constitution or laws of the United States must be an element, *and an essential one,* of the plaintiff's cause of action. * * * The right or immunity must be such that it will be supported if the Constitution or laws of the United States are given one construction or effect, and defeated if they receive another." [Italics supplied]

And further in its opinion this Court said (299 U. S. at pp. 117-118):

> "* * * To define broadly and in the abstract 'a case arising under the Constitution or laws of the United States' has hazards of a kindred order. What is needed is something of that common-sense accommodation of judgment to kaleidoscopic situations which characterizes the law in its treatment of problems of causation. One could carry the search for causes backward, almost without end. * * * Instead there has been a selective process *which picks the substantial causes out of the web and lays the other ones aside.* As in problems of causation, so herein the search for the underlying law. If we follow the ascent far enough, countless claims of right can be discovered to have their source or their operative limits in the provisions of a federal statute or in the Constitution with its circumambient restrictions upon legislative power. To set bounds to the pursuit, the courts have formulated *the distinction between controversies that are basic and those that are collateral,* between disputes that are necessary and

> those that are merely possible. We shall be lost in a maze if we put that compass by." [Italics supplied]

It appears clear to us that, in the language of the *Gully* case, the alleged violation of Section 5 of the Transportation Act (49 U. S. C. § 5) is not "an element, and an essential one" of the second cause of action. Neither the intention of the pleader nor the expedient of alleging identical facts under two causes of action can alter the conclusion that the federal claim is "collateral" not "basic".

Applying the *Gully* doctrine to the complaint before it, the District Court correctly concluded that (R. 314-315):

> "* * * Insofar as the pleading of the second count there is no real difference in either complaint. Fraud, inadequacy of consideration for transfer of assets of Ogden and the despoilment of Ogden to the benefit of the defendants are the gravamen of both counts of each complaint. * * *
>
> "The wrong alleged is a corrupt agreement and unlawful conspiracy to defraud and despoil Ogden of valuable properties. The perpetration of this wrong and the acts committed to achieve its consummation embrace a violation of a federal statute. * * * The violation of the federal statute is but an incident to the wrongful acts alleged to have been committed."

An analysis of the complaint supports the conclusion of the District Court that there is "no real difference" between the first and second counts. In both causes of action, the essential claim is that the defendants in breach of their fiduciary duties caused Ogden to part with valuable assets for an allegedly inadequate consideration. The loss caused Ogden, if any, was occasioned, not by the failure of the defendant Holtzmann to secure the approval of the Interstate Commerce Commission to the transfer, but was due to the transfer of the properties for what is alleged to have been an inadequate consideration. Under such

circumstances, whether Holtzmann's acquisition of Litchfield without the prior approval of the Interstate Commerce Commission constituted a violation of the Transportation Act is obviously immaterial, for in the absence of inadequacy of consideration Ogden would have no cause for complaint.

As the District Court correctly stated (R. 316), "the success of plaintiffs in their suit will not be sustained if the Constitution and laws of the United States are given one construction, and defeated if given another."*

A recent and pertinent illustration of the requirement that a claimed violation of a federal statute must be "an element, and an essential one" of the claim asserted is found in *Andersen* v. *Bingham & G. Ry. Co.*, 169 F. 2d 328 (10th Cir. 1948). That case involved an action initially instituted in a State court for personal injuries sustained as a result of a collision between an automobile driven by the plaintiff and a train operated by the defendant. As an element of negligence it was alleged that the train was being operated with inefficient and inadequate brakes in violation of Section 1 of the Safety Appliance Act, as amended (45 U. S. C. § 1). The case was removed to the federal court at the instance of the defendant, and over the objection of the plaintiff, upon the theory that the suit was one arising under the laws of the United States.

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* That the Court below merely accepted the pleaders' conclusion that the second cause of action was based upon the alleged violation of Section 5 of the Transportation Act without considering the provisions of that Section is apparent. The prohibitions of that Section "are directed to the *purchaser* of the property" (*Erie R. Co., Purchase,* 54 I. C. C. 486, 490, 49 U. S. C. § 5(2)), not the seller. Accordingly, the claim that Ogden, or its officers and directors, somehow violated the Section by failing to secure Commission approval is wholly frivolous. They were not required by the terms of the Section to secure approval, and had they sought such approval the Commission would not have entertained the application (*Erie R. Co., Purchase, ibid.*).

On appeal, the Court of Appeals, relying upon the *Gully* case, reversed the judgment and remanded the case to the District Court with directions to remand the case to the State Court. The Court of Appeals, in holding that the alleged violation of the federal statute was not an "essential" element of a cause of action which had its "genesis" in State law, said (169 F. 2d at 330-331):

> "The allegations in the complaint charging as an element of negligence failure on the part of the defendant to comply with the exactions of the Safety Appliance Act merely tendered the issue of fact whether the train was operated without brakes being in operative condition as required by the Act. The complaint did not present any issue or controversy in respect to the validity, construction, or effect of the Act. It did not set forth any right or immunity which would be supported if the Act be given one construction or effect and defeated if given another. While the pertinent provisions of the Act lurked in the background as creating a duty the breach of which constituted negligence, the right of action available and the incidents of such right of action sprang from the law of Utah. It did not arise under the laws of the United States. * * *"

Accord: *Oldland* v. *Gray*, 179 F. 2d 408 (10th Cir. 1950).

So, too, in the instant case, the alleged violation of the Transportation Act merely tenders the issue as to whether the Act was violated as an incident of the breach by the defendants of their fiduciary duties. The complaint states a cause of action having its "genesis" in State law and not one arising under the laws of the United States.

Almost the precise basis of federal jurisdiction claimed here by the respondents was asserted and denied in the comparatively recent case of *Downing* v. *Howard*, 68 F. Supp. 6, aff'd. 162 F. 2d 654 (3rd Cir. 1947), cert. den. 332 U. S. 818 (1947). Indeed, the Court below has recognized the inconsistency of its holding with the result reached in that case (R. 125).

In the *Downing* case, a stockholders' derivative action was brought to recover from former and present directors and third parties, alleged to have acted in conspiracy, approximately $100,000,000 for waste of assets caused by the alleged breach of a fiduciary duty and for an accounting. Jurisdiction was predicated upon an alleged violation of Section 25 of the Public Utility Holding Company Act of 1935. In dismissing the suit for lack of federal jurisdiction, the District Court held (68 F. Supp., at p. 10):

> "* * * Absent other jurisdictional elements, a minority stockholder may not resort to the federal courts on simple allegations that directors and officers, with other co-conspirators, have violated federal statutes—such as anti-trust laws and the Interstate Commerce Act, 49 U. S. C. A. § 1 et seq.—in addition to committing breaches of fiduciary duty. * * *"

See also, *Meyer* v. *Kansas City Southern Ry. Co.*, 11 F. Supp. 937, aff'd 84 F. 2d 411 (2d Cir. 1936), cert. den. 299 U. S. 607 (1936).

POINT II

The Court of Appeals incorrectly interpreted and applied this Court's holding in *Cohen* v. *Beneficial Industrial Loan Corporation*, 337 U. S. 541 (1949).

In the face of the ruling of this Court in *Cohen* v. *Beneficial Industrial Loan Corporation*, 337 U. S. 541 (1949), the Court below expressly recognized that its opinion was "not free from doubt" (R. 127). Apparently, the Court of Appeals recognized that its decision constituted an impairment of what this Court had characterized as a state's plenary regulatory powers over the internal relations between corporate management and stockholders (337 U. S. at pp. 549, 550).

In the *Cohen* case this Court, in discussing the applicability in the federal court of a New Jersey statute, requiring the plaintiffs in a stockholders' derivative action to give security for expenses, similar in all respects to Section 61-b of the New York General Corporation Law, first quoted the Rules of Decision Act (28 U. S. C. § 1652), providing as follows:

> "The laws of the several states, except where the Constitution or treaties of the United States or Acts of Congress otherwise require or provide, shall be regarded as rules of decision in civil actions in the courts of the United States, in cases where they apply. June 25, 1948, c. 646, 62 Stat. 944."

It then proceeded to hold that the New Jersey security statute created a "substantive" regulation applicable to stockholders' derivative actions instituted in the federal district courts sitting in New Jersey, and that the District Court in that case had erred in declining to fix the amount of security to be furnished. The holding of this Court was stated as follows (337 U. S. at p. 557):

> "We hold that the New Jersey statute applies in federal courts and that the District Court erred in declining to fix the amount of indemnity reasonably to be exacted as a condition of further prosecution of the suit."

The Court below gave controlling effect to the decision of this Court in the *Cohen* case with respect to the first cause of action pleaded in the complaint at bar, in which jurisdiction of the federal court was based solely upon diversity of citizenship, but it denied the applicability of the decision to the second cause of action, where the wrongdoing was alleged to involve incidentally a violation of a federal statute. To reach this anomalous result, the Court of Appeals described the second cause of action as one "based on a law of the United States", and treated the pleaders' essential jurisdictional allegation of "diversity"

as "a defect in pleading which may be disregarded as surplusage".

Whether or not the plaintiffs in their second cause of action have also alleged a violation of a federal law, that circumstance does not, we submit, logically render Section 61-b of the New York General Corporation Law inapplicable to the second cause of action pleaded in the complaint.

The *Cohen* case, as is the case at bar, was a stockholders' derivative action instituted in the right of a Delaware corporation against officers and directors for alleged breach of their fiduciary duties. In the *Cohen* case, as in the second cause of action in the complaint at bar, jurisdiction of the federal court was invoked upon the grounds of diversity of citizenship. The identity of these cases, we submit, clearly dictates that, if a State-declared policy of requiring the plaintiffs in a stockholders' derivative action to give security for expenses is to be given effect in one instance, it should also be given effect in the other.

In *Erie R. Co.* v. *Tompkins*, 304 U. S. 64, 78 (1938), this Court laid down the applicable rule as follows:

> "* * * Except in matters governed by the Federal Constitution or by Acts of Congress, the law to be applied in any case is the law of the State."

While it is true that in the *Erie* case, *supra*, applying State decisional law, in the later case of *Guaranty Trust Co.* v. *York*, 326 U. S. 99 (1945), applying the New York statute of limitations in an equity action, and in the still later *Cohen* case, *supra*, jurisdiction of the federal court was based only upon diversity of citizenship, the holdings of these cases may not properly be interpreted to mean that federal courts will apply State law only in cases where diversity is the *sole* asserted ground of jurisdiction (see, in this connection, 3 Cyclopedia of Federal Procedure § 639 (2d ed. 1943); Comment 5 Mo. L. Rev. 193, 204).

Numerous examples may be cited where, in the absence of controlling federal statutes, State statutory law has been applied although federal jurisdiction was invoked upon grounds other than diversity of citizenship.

Thus, in *Wichita Royalty Co.* v. *City Bank*, 306 U. S. 103 (1939), decided shortly after the *Erie* case, *supra*, this Court appears to us to have held that it was the duty of the federal court to apply State decisional law in a case where jurisdiction was based not upon diversity, but upon the National Banking Act.

In *Cope* v. *Anderson*, 331 U. S. 461 (1947), where there was no federal statute of limitations fixing the period within which suits must be brought to enforce the statutory double liability of shareholders of insolvent national banks, this Court held the State statute of limitations applicable in suits brought by a receiver.

A similar result has also been reached in suits for treble damages under the anti-trust laws (*Chattanooga Foundry and Pipe Works* v. *Atlanta*, 203 U. S. 390 [1906]), in suits for the deprivation of civil rights or for conspiracy to deprive persons of civil rights (*O'Sullivan* v. *Felix*, 233 U. S. 318 [1914]), and in actions arising out of copyright infringement (see *Brady* v. *Daly*, 175 U. S. 148 [1899]).

In cases arising under the Bankruptcy Act, where the question has been whether the parties filing the petition had the right to do so, this Court and the lower federal courts have recognized that, in the absence of an otherwise controlling federal statute, such a question is to be determined by State law (see *Price* v. *Gurney*, 324 U. S. 100 [1945]; *In re Camp Glass Casket Co.*, 272 Fed. 558 [6th Cir. 1921]). So also, in a suit for damages for death under a specially enacted federal statute, the question of whether the plaintiff was entitled to sue was determined under State law (*U. S.* v. *Durrance et al.*, 101 F. 2d 109 [5th Cir. 1939]).

In the case at bar, State law requires that, lacking requisite stock ownership, the plaintiffs in a stockholders' derivative action must post security as a condition of their right to sue upon a corporate cause of action. Such a State-declared policy, in the absence of controlling federal statutes, should be given effect in the federal courts, and we submit that the Court below erred in restricting the applicability of Section 61-b of the New York General Corporation Law solely to the first cause of action alleged in the complaint. So to restrict the applicability of the security statute to causes of action in a derivative stockholders' action instituted in the federal courts is to nullify State-declared policy and encourage the institution of such suits in the federal courts in every instance where, incidentally to the alleged wrongdoing, the plaintiffs may point to the claimed violation of some federal statute.

Conclusion

It is respectfully submitted that the petition of Ogden Corporation for certiorari to review the decision of the United States Court of Appeals for the Second Circuit should in all respects be granted.

Richard Joyce Smith,
Counsel for Petitioner.

Henry S. Reeder,
Bernard L. Sanoff,
of Counsel.

Dated: June 7, 1950.

JUL 24 1950
CHARLES ELMORE CROPLEY
CLERK

Supreme Court of the United States

OCTOBER TERM, 1949

No. 116

BENNETT I. FIELDING and FRANCES BARRETTA, suing on behalf of themselves and all other stockholders of OGDEN CORPORATION who may join in and contribute to the expenses of this action, for and on behalf of OGDEN CORPORATION,

Respondents,

EDWARD A. MILLER and MARY MILLER,

Respondents-Intervenors,

IRVING W. MENCHER,

Respondent-Intervenor,

against

OGDEN CORPORATION,

Petitioner,

and

CHARLES ALLEN, JR., RITA ALLEN, HAROLD ALLEN and SAMUEL ELGORT, individually and as co-partners doing business under the firm name and style of ALLEN AND COMPANY, JACOB L. HOLTZMANN, LILLIAN HOLTZMANN, BENJAMIN H. BREWSTER, LEON COLE, L. BOYD HATCH, MAURICE L. SINDEBAND, LILLIAN SINDEBAND, HOWARD L. FOGG, RALPH B. DURELL, Executor of the Last Will and Testament of Thomas P. Durell, deceased,

Defendants,

and

HELEN S. FOGG and C. W. RETNAUER,

Defendants.

ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF IN OPPOSITION ON BEHALF OF RESPONDENTS

MORTIMER HAYS.
Counsel for Respondents.

MORTIMER FEUER,
of Counsel.

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Supreme Court of the United States

OCTOBER TERM, 1949

No. 116

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IRVING W. MENCHER,

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against

OGDEN CORPORATION,

Petitioner,

and

CHARLES ALLEN, JR., RITA ALLEN, HAROLD ALLEN and SAMUEL ELGORT, individually and as co-partners doing business under the firm name and style of ALLEN AND COMPANY, JACOB L. HOLTZMANN, LILLIAN HOLTZMANN, BENJAMIN H. BREWSTER, LEON COLE, L. BOYD HATCH, MAURICE L. SINDEBAND, LILLIAN SINDEBAND, HOWARD L. FOGG, RALPH B. DURELL, Executor of the Last Will and Testament of Thomas P. Durell, deceased,

Defendants,

and

HELEN S. FOGG and C. W. RETNAUER,

Defendants.

RESPONDENTS' BRIEF

The order of the Court of Appeals, Second Circuit, (1) affirmed an order of the District Court in so far as it required the posting of security under Section 61-b of the New York General Corporation Law with respect to the

first cause of action in the complaint—as to which Federal jurisdiction was invoked on the ground of diversity of citizenship, and (2) reversed said order in so far as it required the posting of security with respect to the second cause of action, which is predicated upon, and claims a right to recover under, the Transportation Act (R. 129).

Petitioner seeks a writ of certiorari to review so much of the order of the Court of Appeals as reversed the order of the District Court.

The opinion of the Court of Appeals (R. 120-128) is reported in 181 F. (2d) 163. That of the District Court (R. 99-110) is not officially reported.

Statutes Involved

The petition (pp. 2, 3), in listing statutes involved, omitted mention of the statute upon which the second cause of action in the complaint is founded (R. 21, 22), namely, the Transportation [or Interstate Commerce] Act, as amended, 49 U. S. C. Sec. 5, Par. (4) and Par. (2) (a)(i).

Sec. 5, Par. (4) provides:

> "(4) It shall be unlawful for any person, except as provided in paragraph (2), to enter into any transaction within the scope of subparagraph (a) thereof, or to accomplish or effectuate, or to participate in accomplishing or effectuating, the control or management in a common interest of any two or more carriers, however such result is attained, whether directly or indirectly, by use of common directors, officers, or stockholders, a holding or investment company or companies, a voting trust or trusts, or in any other manner whatsoever. It shall be unlawful to continue to maintain control or management accomplished or effectuated after the enactment of this

amendatory paragraph and in violation of its provisions. As used in this paragraph and paragraph (5), the words 'control or management' shall be construed to include the power to exercise control or management."

Sec. 5, Par. (2)(a) [referred to in Par. 4, supra] provides in part:

"(2) (a) It shall be lawful, with the approval and authorization of the Commission, as provided in subdivision (b)—

(i) * * * for a person which is not a carrier to acquire control of two or more carriers through ownership of their stock or otherwise; or for a person which is not a carrier and which has control of one or more carriers to acquire control of another carrier through ownership of its stock or otherwise;"

Summary Statement of Case

The complaint in this stockholders' derivative suit, brought on behalf of the Ogden Corporation sets forth two causes of action (R. 5-26). Diversity of citizenship exists as between plaintiff Fielding, who instituted the action,* and the defendants, and the first cause, alleging that corporate assets viz., the stock of a railroad company, the stock of a coal company, an indebtedness from the coal company to Ogden, were sold for a grossly inadequate price and charging defendants with conspiracy, fraud and (as to Ogden directors) breach of fiduciary duties, invokes Federal jurisdiction on the ground of such diversity (R. 19).

* A consolidation with the Barretta action and interventions by other plaintiffs followed (R. 1-3).

The second cause of action, however, relates only to the sale of the stock of the railroad company, repeats by reference allegations of the first cause with respect to such "carrier," sets forth the relevant sections of the Transportation Act, and then sets forth the facts showing the violation of the Act, predicating the right to relief thereon. The jurisdictional allegation states that said second cause arises under the laws of the United States, the Transportation Act, "as hereinabove more fully appears, and jurisdiction of this Court depends thereon," and then adds "as well as on diversity of citizenship" (R. 25). [This addition was properly characterized as "surplusage" by the Court below (181 F. [2d] at 166; R. 124)].

This Court in *Cohen* v. *Beneficial Industrial Loan Corp.*, 337 U. S. 541 (1949) had determined, in a case where the Federal Court had jurisdiction "only because the parties are of diverse citizenship," that a New Jersey statute similar to Sec. 61-b was constitutional, was substantive and was applicable.

In the instant case, the Court of Appeals accorded full effect to that decision and held—as indeed respondents (appellants in that Court) had conceded—that it was applicable to the first cause of action, since jurisdiction as to that cause was invoked on the ground of diversity of citizenship; and as to that cause it affirmed the ruling of the District Court requiring the posting of security under Sec. 61-b (181 F. [2d] at 165; R. 121-2).

However, as to the second cause, the Court of Appeals held that, since "the complaint raises a question which will be decided favorably or unfavorably to the plaintiffs, depending on the construction given to the Transportation Act," and that this question was raised not with "frivolous purpose" but "fairly" (181 F. [2d] at 166-7; R. 125-6), jurisdiction of the Federal Court was founded

upon a claim under the Federal statute; and that, therefore, said cause was "not subject to special requirements for cognate actions under state law," and plaintiffs should not have been required to furnish security under Section 61(b) as a condition to its prosecution (181 F. [2d] at 168; R. 127).

As to the decision by this Court in the *Cohen* case, the Court of Appeals pointed out that this Court "was dealing with a diversity case, and we believe the decision must be limited to that situation," citing in that behalf several other authoritative decisions by this Court (181 F. [2d] at 168; R. 128).

The Complaint

The question presented here by petitioner relates only to the second cause, but a summary of the allegations of both causes is helpful, as underscoring the pleader's determination, as to the second cause, to rely upon and maintain the suit under the Transportation Act.

First Cause

Ogden Corporation owned all the stock of Litchfield & Madison Railway Company, and all the stock of Mt. Olive & Staunton Coal Company (R. 9). The stock of both Litchfield and Mt. Olive, and also a large indebtedness ($1,162,844) owing by Mt. Olive to Ogden Corporation was sold by Ogden to defendant Holtzmann who [for reasons set forth in the second cause of action] acted as an agent and dummy for defendants Allen & Co., a partnership. Ogden received for the Litchfield stock, preferred and common, $1,440,000 and for the Mt. Olive stock and indebtedness, $310,000, the total (with interest) being $1,758,883 (R. 13, 14).

Facts and figures are detailed in the complaint to show: That the Litchfield preferred had regularly received its

$4 dividend; that in effect, only $950,000 was paid for the Litchfield common which had earned and received approximately $500,000 yearly in dividends for the five years next preceding the sale; and that the coal company (Mt. Olive) was so profitable that within two years it paid out to the purchasers, on account of its indebtedness, more than the $310,000 that they had paid to acquire the coal company stock and indebtedness. Allen & Co. retained (i. e. received by "assignment" from Holtzmann) 70% of the assets acquired (other than the Litchfield preferred which was sold to an insurance company), the balance going to Holtzmann, directors and officers of Ogden, and some others (R. 9-17).

It is alleged that Ogden's holdings in Litchfield had a real value of about $6,125,000 and its holdings in Mt. Olive had a real value of about $1,500,000 (R. 12, 13); that the price received for these assets, namely $1,758,883.33 was grossly inadequate (R. 14) and facts, additional to those above referred to, are alleged (R. 17) which substantiate the charge that the sale was contrary to Ogden's interest and that the acquisition of the assets by Allen & Co. (through Holtzmann) was pursuant to a fraudulent conspiracy with the officers and directors of Ogden, some of whom participated in the fruits of the fraud.

Second Cause

This cause deals only (and not merely "more particularly"; see petition, p. 7) with the sale by Ogden of the Litchfield stock, its scope being so restricted because only the sale of the stock of the Litchfield Railway was subject to the Transportation Act and consummated in violation thereof.

This cause sets forth at length the pertinent provisions of the Act (R. 21-2) also quoted supra, pp. 2, 3. In substance they are that unless approval and authorization,

by order of the Interstate Commerce Commission, is obtained, it is "unlawful for any person * * * to accomplish or effectuate, or to participate in accomplishing or effectuating the control or management in a common interest of any two or more carriers, however such result is attained, whether directly or indirectly, * * *."

This cause goes on to allege facts (not set forth in the first cause) which support the charge of violation of the Transportation Act. It is alleged that Allen & Company was at the time of the transaction the owner of 68¼% of the stock of The Cincinnati, Newport & Covington Railway, a carrier within the terms of the Transportation Act, and that any further acquisition by or on behalf of Allen & Co. of the control of another carrier (*e. g.*, Litchfield) would require approval and authorization by the Interstate Commerce Commission. In connection, moreover, with any hearing by the Commission, upon any proposed sale by Ogden to Allen & Co., inquiry would have been made into the fairness and reasonableness of the terms of the proposed transaction, particularly from the point of view of Ogden stockholders* (R. 22). In order to evade such inquiry, defendants conceived the device of using Holtzmann as a purported principal, and since Holtzmann himself was not in control of any other carrier, the sale by Ogden to him of the Litchfield stock was not submitted for Commission approval, although it should have been since Holtzmann was acting as the agent and dummy for Allen & Co. (R. 23).

The subsequent purely formal assignment of the controlling block of Litchfield stock from Holtzmann to Allen & Co. was submitted for Commission approval. But since this assignment purported to be merely a transfer by defendant Holtzmann as principal to defendants Allen &

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* See *U. S.* v. *Lowden*, 308 U. S. 225, 233 fn. 1 (1939).

Co., there was no apparent basis for inquiry into the fairness of the terms and there was, of course, no inquiry into the fairness and reasonableness of the terms of the transaction from the point of view of Ogden and its stockholders. There was concealed from the Commission the fact that Holtzmann had acted as the agent of Allen & Co. in acquiring the Litchfield stock from Ogden (R. 23, 24).

It is accordingly alleged that the transaction by which Ogden was divested of and Allen & Co. acquired control of Litchfield was unlawful and void (R. 24).

Relief, by way of rescission of the sale and a reconveyance to Ogden of the assets unlawfully transferred to defendants, and an accounting, is specifically requested (R. 24).

Summary of Argument

The two points urged by petitioner are in substance:

(1) That the allegations of the second cause of violation of the Transportation Act are non-essential and sham or frivolous and that they add nothing to the charges in the first cause; that jurisdiction over the second cause, like the second, is necessarily predicated upon diversity of citizenship, and that therefore substantive state law (New York General Corporation Law, § 61-b) is applicable to said second cause, in the same manner as it was held applicable to the first. Upon the assumption that the allegations of the violation of the Federal Act are non-essential and immaterial, it is urged that the determination by the Court of Appeals, that the claims asserted in the second cause are federal in nature and that jurisdiction was properly predicated thereon, was erroneous and in conflict with *Gully* v. *First National Bank,* 299 U. S. 109 (1936).

(2) That even if a federal claim is asserted by the second cause and the jurisdiction of the Federal Court is

predicated thereon (independently of diversity of citizenship), nevertheless the decision of this Court in the *Cohen* v. *Beneficial Industrial Loan Corp.*, 337 U. S. 541 (1949) requires that state substantive law (§ 61-b) be followed and applied.

It is respectfully submitted, however, that the premise of petitioner's first point, namely, that the allegations of violation of the federal statute are non-essential and sham and frivolous, is without warrant, and the petitioner's conclusion therein baseless; and that, as to petitioner's second point, the Court of Appeals properly held that the *Cohen* case was—as this Court itself indicated—limited to a situation in which the jurisdiction of the Federal Court was predicated upon diversity of citizenship. The purported conflicts with the *Gully* and *Cohen* decisions are non-existent.

ARGUMENT

POINT I

The Court of Appeals in rendering its decision accorded full recognition to the principles of *Gully* v. *First National Bank*, 299 U. S. 109 (1936) and Petitioner's claim of "conflict" is without basis. (Answering Pet. Br., Point I, pp. 11, *et seq.*)

In the *Gully* case action was brought in the Mississippi State Court by the State Tax Collector to recover state, county, city and school district taxes owed by defendant, a national bank. Defendant removed the case to the Federal Court, and the Court of Appeals held properly so, on the ground that the power to impose taxes on national banks was granted by federal statute, and that therefore, by necessary implication, plaintiff in suing for the taxes relied upon the statute. This Court held, however, revers-

ing the Court of Appeals decision, that the only effect of the federal statute was to deprive the bank of a defense to the action that it might otherwise have had and that "a suit does not arise under a law renouncing a defense" (p. 116).

In making this holding the Court referred to the principle that, for a case to arise under the Constitution or Laws of the United States, the right or immunity created by the Constitution or Laws muse be an "essential" element of plaintiff's claim. Petitioner here relies upon this principle and urges (Pet. Br., p. 11) that it was "ignored" by the court below in making its decision.

The court below, however, not only did not ignore the principle, but specifically adverted to the aspects of the plaintiff's second cause which demonstrate that the claims therein are necessarily predicated upon the Transportation Act. Thus it stated (181 Fed. [2d] at 166, 167; R. 124-5):

> "The count sets up the Transportation Act and alleges that its requirement of approval by the Interstate Commerce Commission was violated by transferring the Litchfield stock to Allen & Company through an intermediary. It asserts that the Commission's approval of the transfer from Holtzmann was obtained by the suppression of material facts and is void. Under the latter charge the claim may be considered as one to compel Ogden Corporation to apply to the Commission to reopen the hearing at which its approval was obtained. That is a claim under a federal statute whether or not Ogden Corporation has any standing to apply for such reopening. It is true that the count does not request a reopening, but probably such relief would be appropriate under the general prayer for 'such other and further relief as may be just and proper in the premises,' and, if not, the request could be reframed. Moreover, just as it stands, the count asks for a rescission of the sale and

a reconveyance to Ogden Corporation of all the assets unlawfully transferred to the defendants. With respect to Litchfield stock that also is a claim under the statute. Nor is it a mere repetition of the first count, since if the Transportation Act was violated, as charged, it may be that Ogden Corporation can rescind the sale even though the consideration received for Litchfield stock was not so inadequate as to prove a breach of fiduciary duty by the directors in authorizing the sale. Viewed either way, the complaint raises a question which will be decided favorably or unfavorably to the plaintiffs depending on the construction given to the Transportation Act. That is the essence of a federal question from the jurisdictional standpoint.* We do not, of course, express any opinion as to the merits of the claims asserted. We merely affirm their federal nature."

The Court also pointed out that the instant situation was not one in which the cause presented a federal question "for the frivolous purpose of obtaining federal jurisdiction, which would otherwise have been lacking", but that: "Plaintiff has fairly raised a question under the Transportation Act" (181 Fed. [2d] at p. 167; R. 126).

It is noteworthy that although petitioner asserts that the Court of Appeals ignored the principle of the *Gully* case, nowhere in its petition or brief does it attempt to answer the points made by the Court demonstrating that the second cause clearly presents federal questions within the meaning of that principle.

Instead petitioner urges (Pet. Br., pp. 8, 11) that the claimed violation of the federal statute was only "incidental" to what it describes as the "essential" claim for an accounting for breach of fiduciary duties by corporate

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* Citing the *Gully* case, and also *Bell* v. *Hood*, 327 U. S. 678, 685.

officers and directors. The apparent basis for petitioner's assertion is that, preliminary to the specific allegations of the second cause, which relate exclusively to the claims under the Transportation Act, that cause formally repeats by reference those allegations of the first cause, including those of breach of fiduciary duty, which relate to Litchfield (see Pet. Br., pp. 6, 7). Petitioner urges, too, that the Transportation Act does not provide for a private right of action for its violation, and, therefore, the right to maintain the action is not "federally conferred" (Pet. Br., p. 13).

In substance, therefore, petitioner's arguments are:

1. That (by virtue of the formal repetition) the second cause contains allegations which purport to state a cause under common law principles and, therefore, the claims under the federal statute are to be disregarded as immaterial or non-essential for jurisdictional purposes.

2. In any event the claims under the federal statute are insufficient as a matter of law and that, therefore, jurisdiction cannot be predicated thereon.

But these self-same contentions were presented to and rejected by this Court in *Bell* v. *Hood,* 327 U. S. 678 (1946). This Court there held:

I. The "party who brings a suit is master to decide what law he will rely upon", and where it is apparent that the pleader's purpose was to claim a right to recover under the Constitution or laws of the United States, and such claim is fairly and not frivolously made, federal jurisdiction is properly invoked on that ground, and the circumstance that the allegations also state "a common law action * * * made actionable by state law" is of no significance and does *not* render the allegations of violation of the federal Constitution or laws "immaterial" (pp. 681,

683). Indeed, in the case before it, and despite the fact that the allegations also stated a cause actionable by state law, the Court concluded, from the apparent purpose of the pleader and the manner in which the complaint was framed, that the alleged violations of the Constitution were not only material, "but form rather the sole basis of the relief sought" (p. 683).

II. "Jurisdiction * * * is not defeated * * * by the possibility that the averments might fail to state a cause of action on which petitioners could actually recover. For it is well settled that the failure to state a proper cause of action calls for a judgment on the merits and not for a dismissal for want of jurisdiction. Whether the complaint states a cause of action on which relief could be granted is a question of law and just as issues of fact it must be decided after and not before the court has assumed jurisdiction over the controversy" (p. 682).

In the instant case the determination of the pleader to predicate the second cause upon the violation of the Transportation Act is amply indicated: (a) by the limitation of its scope to the sale and acquisition of the Litchfield stock; (b) by the specific allegations of the second cause, all of which deal with the facts that demonstrate violation of the Act; (c) by the fact that a second cause was stated at all [Petitioner's contention, if sustained, would make the second cause merely a senseless repetition, with respect to the Litchfield stock, of the first cause]; and finally (d) by the fact that under the second cause issues are fairly presented under the Transportation Act, the resolution of which may well afford plaintiffs the right to relief which could not be obtained under the claim of breach of fiduciary duties, etc. in the first cause (see quotation from opinion by the Court below, *supra*, pp. 10, 11).

The Court of Appeals, moreover, properly concluded that the issues or questions under the Transportation Act

were presented fairly and not with frivolous design.* It pointed out that under the decision in *Bell* v. *Hood* it was not necessary that the "federal statute upon which the claim is based expressly provide that the plaintiff shall have a remedy by way of suit" (181 Fed. [2d] at 166; R. 124). It referred to the questions presented which, if resolved in plaintiff's favor, would afford relief which could not be obtained in the absence of a violation of the Transportation Act. Of course, it made no determination of the merits of these claims, since under the *Bell* case and the authorities cited therein, including the leading case of *The Fair* v. *Kohler Dye & Specialty Co.*, 228 U. S. 22, the jurisdiction question was not properly determinable in terms of the merits.**

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* Petitioner argues (Pet. Br., p. 16 fn.) that the prohibitions of Section 5 "are directed to the purchaser of the property" and accordingly any claim that Ogden "or its officers and directors somehow violated the Section by failing to secure Commission approval is wholly frivolous". In making this statement petitioner wholly disregards the provisions of Section 5, Par. (4) [quoted *supra*, p. 2], that unless approval and authorization of the Commission is obtained it is *"unlawful for any person* * * * to accomplish or effectuate, or *to participate in accomplishing or effectuating* the control or management in a common interest of any two or more carriers * * *". The allegations of conspiracy, etc. [see pars. 26 (R. 20) and 36 (R. 24) of the second cause which repeat by reference the allegations of pars. 16 (R. 13) and 20 (R. 18)] clearly connect the officers and directors as participants in the unlawful conduct and accordingly as violators of the Act.

** Petitioner's brief (fn. p. 13) suggests that "No case is found in which the Courts have sustained a private right of action" for violation of the Transportation Act and that under analogous statutes the existence of such right has been denied. But in *Norfolk Southern Bus Corp.* v. *Virginia Dare Transp. Co., Inc.*, 159 Fed. (2d) 306 (C. C. A. 4th, 1947), cert. den. 331 U. S. 827 (1947), the Court made a determination "that it was unlawful for the parties hereto to enter into the contract except upon the specific approval by order of the Commission * * *. The agreement should have been submitted to the approval of the Commission * * * and since it was not, it fell within the interdiction of the statute, and was therefore unlawful and void" (p.

(*Footnote continued on next page*)

It may be observed that the Court below, in view of the *Bell* case and the cases on which it relied, stated (181 Fed. [2d] at 167; R. 125) it could not follow the decision in *Downing* v. *Howard,* 162 Fed. (2d) 654 (C. C. A. 3rd, 1947), cert. den. 332 U. S. 818, in which the court felt (see fn. 3 at p. 655) that in determining the jurisdictional question, it was encumbent upon it to decide whether a sufficient cause of action was stated under the federal statute. Petitioner seemingly suggests that the refusal to follow the *Downing* case *in that respect* is significant (Pet. Br., p. 17), apparently disregarding entirely the square holding by this Court in *Bell* v. *Hood* and those of the cases cited therein which, as heretofore indicated, make it abundantly clear that there should at most be determined, in deciding the jurisdictional question, that federal issues are not frivolously presented and that further inquiry into the merits is not warranted.

Petitioner quotes from the opinion of the District Court in the *Downing* case upon a matter in which the Court of Appeals in that case ruled differently and adversely to petitioner's contention. The portion of the opinion of the District Court to which reference is made (Pet. Br., p. 18) is to the effect that federal jurisdiction may not be invoked where a cause contains allegations showing *both* vio-

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(*Footnote continued from preceding page*)

311). In that case the Court denied relief to both parties to the contract as being "in *pari delicto*", a principle which, however, would be inapplicable to the present suit. *Goldstein* v. *Groesbeck,* 142 Fed. (2d) 422, 427 (C. C. A. 2nd, 1944), cert. den. 323 U. S. 737.

Petitioner argued below that the Commission had exclusive jurisdiction over claimed violations of § 5 of the Transportation Act. But such question of "exclusive jurisdiction" is in reality a question relating to the merits. *General Invest. Co.* v. *N. Y. C. R. Co.,* 271 U. S. 228, 230 (1926). Moreover, the *Norfolk* case sufficiently illustrates that the situation here involved is (in the language of *Armour & Co.* v. *Alton Railroad Co.,* 111 Fed. (2d) 913 (C. C. A. 7th, 1940), affd. 312 U. S. 195) one in which "original resort to the courts" is permissible and in which "prior administrative adjudication" is unnecessary (111 Fed. [2d] at 917).

lations of federal statutes *and* breaches of fiduciary duty. But the manner in which the Court of Appeals in the *Downing* case posed the problem before it showed that it disagreed with that statement of the District Court. Thus it said (p. 655):

> "It is apparent that the question which we have to settle is whether the plaintiff has stated a basis for recovery under the federal statute just mentioned. If he has, the fact that he also asserts a non-federal ground does not lose him his privilege of suing in the federal court."

If, for the language "has stated a basis" in the above quotation [implying a requirement of a decision on the merits], there is substituted "has fairly, and not frivolously, presented a claim", the statement by the Court would be in accord with the decision by this Court in *Bell* v. *Hood,* for, as already noted in the *Bell* case it was held also that if plaintiff fairly presents a claim under the Constitution or laws of the United States, the fact that the allegations also state a cause actionable under State law does not lose the plaintiff his privilege of suing in the Federal Court.*

It is respectfully submitted that in determining that the claims of the second cause were federal in nature, and that jurisdiction was properly invoked on that ground, the Court below properly applied the principles of both the *Bell* and *Gully* cases.

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* See to like effect—following *Bell* v. *Hood*—the case of *Stella* v. *Kaiser,* 82 Fed. Supp. 301 (S. D. N. Y., 1948).

POINT II

The Court of Appeals correctly interpreted and applied the ruling of *Cohen* v. *Beneficial Industrial Loan Corp.*, 337 U. S. 541 (1949). (Answering Pet. Br., Point II, pp. 18, *et seq.*)

The holding by the Court below, that § 61-b was applicable to the first but not the second cause, was clearly correct under the *Cohen* decision. In requiring the furnishing of security under the New Jersey statute, similar to § 61-b, this Court in the *Cohen* case made it plain that it was dealing with a case in which the Federal Court had jurisdiction "only because the parties are of diverse citizenship." The inference from that case was clear that the State statute would not be applied in a situation in which the Federal Court's jurisdiction did not depend on diversity.

At the very outset, the opinion in the *Cohen* case (per Mr. Justice Jackson) states (p. 543):

> "The ultimate question here is whether a federal court, *having jurisdiction of a stockholder's derivative action only because the parties are of diverse citizenship,* must apply a statute of the forum state which makes the plaintiff, if unsuccessful, liable for the reasonable expenses, including attorney's fees, of the defense and entitles the corporation to require security for their payment." (Italics added.)

Discussing the applicability of the statute the Court pointed out that "*in diversity cases* the federal court administers the state system of law" (p. 555). In this connection it cited *Guaranty Trust Co.* v. *York,* 326 U. S. 99 (1945) in which the Court pointed out that the intent of the decision in *Erie* v. *Tompkins* (304 U. S. 64) was to insure that "in all cases where a federal court is ex-

ercising jurisdiction *solely* because of the diversity of citizenship of the parties," State law should be applied (326 U. S. at 109).

In the instant case jurisdiction over the second cause is not dependant on diversity. The jurisdictional allegation (Par. 37, R. 25) clearly shows that reliance is placed upon the fact that the cause arises under the laws of the United States, namely, the Transportation Act. The additional stated basis for jurisdiction, namely, diversity of citizenship, records an obvious fact but in no way detracts from the primary basis of the court's jurisdiction and may be regarded (as the Court of Appeals stated) as mere "surplusage" (181 Fed. 2d at 166; R. 124).

In the above references to the *Cohen* and *York* decisions it is respectfully submitted that emphasis is properly placed upon the language restricting their application to situations in which jurisdiction is dependent upon diversity.

In *Angel* v. *Bullington*, 330 U. S. 183 (1947), the court pointed out that where resort is had to a Federal Court "because a federal right is claimed, the limitations upon the courts of a State do not control a federal court sitting in the State" (p. 192).

In *Deitrick* v. *Greaney*, 309 U. S. 190 (1940), the court stated (at pp. 200, 201):

> "But it is the federal statute which condemns as unlawful respondent's acts. The extent and nature of the legal consequences of this condemnation, though left by the statute to judicial determination, are nevertheless to be derived from it and the federal policy which it has adopted, see Jackson County v. United States, No. 14, decided December 18, 1939 [308 U. S. 343, ante., 313, 60 S. Ct. 284] and cases cited. We have recently held that the judicial determination of the legal consequences which flow from acts condemned

as unlawful by the National Bank Act involves decision of a federal, not a state question. Awotin v. Atlas Exch. Nat. Bank, 295 U. S. 209, 79 L. ed. 1393, 55 S. Ct. 674, supra."

See, also:

Clearfield Trust Co. v. United States, 318 U. S. 363 (1943);
Holmberg v. Armbrecht, 327 U. S. 392 (1946).

Petitioner argues, however (Pet. Br., pp. 20, 22) that "State-declared policy" (*i. e.*, § 61-b) should be given effect to the second cause presenting the federal claims, in the same manner as it has been given effect to the first cause. It is respectfully submitted, however, that, as to the second cause, it is "federal policy" that is controlling (see *Deitrick* case, supra). Such federal policy applicable to derivative actions is expressed in the Federal Rules of Civil Procedure (see in this connection the *Cohen* case, 337 U. S. at 549, 550). There is no reason in principle or authority for the application of the state statute to the prosecution of the federal claims.

In making its contentions, petitioner's brief (p. 21) cites a number of cases. But they are not in point, in some instances their substance being erroneously stated.

In the *Wichita* case (306 U. S. 103) the original claims had nothing to do with the Banking Act. The case was removed from the State Court, after the addition of federal claims (see 95 Fed. [2d] 671, 674). The court applied state decisional law to the original claims (see 97 Fed. [2d] 249). The only question before this Court was whether there had been a correct application of such decisional law (306 U. S. at 104).

Cases in which, in the absence of a federal limitations statute, the courts held state limitations statutes applicable, are *sui generis* and, moreover, merely applied state

rules of procedure and not rules of substance. The other cases are similarly not pertinent.*

It is submitted that the Court below correctly held, under the *Cohen* case, that § 61-b (the New York State statute) was applicable only to the first cause and not to the second, with respect to which jurisdiction is predicated upon the federal claims therein set forth, and does not depend upon diversity.**

CONCLUSION

It is respectfully submitted that the petition of Ogden Corporation for certiorari to review the decision below be denied.

Respectfully submitted,

MORTIMER HAYS,
Counsel for Respondents.

MORTIMER FRYER,
Of Counsel.

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* For example, in *Price* v. *Gurney*, 324 U. S. 100, the court merely held that stockholders of a corporation could not institute Chapter X proceedings for their corporation, since under the Bankruptcy Law petitions could be filed only by the corporation itself or by creditors. The court pointed out that local law (since an Ohio Corporation was involved) which vests management of the corporation in its directors and not its stockholders was determinative of the persons authorized to act in the corporation's behalf and, accordingly, when the Bankruptcy Act permitted the corporation to initiate proceedings, the directors must, and the stockholders could not, institute such proceedings for the corporation.

In *U. S.* v. *Dorrance*, 101 Fed. (2d) 109, parents of the claimant were killed in Florida when their car collided with a Department of Agriculture truck. A special statute was enacted waiving U. S. sovereignty immunity from suit and conferring jurisdiction upon a District Court in Florida to entertain it. The court held that it was not the intent of Congress to confer upon claimant any right of action not conferred by Florida law, but only to waive immunity and provide a forum. Under Florida law (common law or statute) plaintiff could not recover since she was an adult, married, did not live with her parents and was not dependent on them for support.

** See also *Stella* v. *Kaiser*, 81 Fed. Supp. 807 (S. D. N. Y., 1948).

SEP 2 1950
CHARLES ELMORE CROPLEY
CLERK

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1949

No. 116

BENNETT I. FIELDING and FRANCES BARRETTA, suing on behalf of themselves and all other stockholders of OGDEN CORPORATION who may join in and contribute to the expenses of this action, for and on behalf of OGDEN CORPORATION,

Respondents,

EDWARD A. MILLER and MARY MILLER,
Respondents-Intervenors,

IRVING W. MENCHER,
Respondent-Intervenor,

against

OGDEN CORPORATION,

Petitioner,

and

CHARLES ALLEN, JR., RITA ALLEN, HAROLD ALLEN and SAMUEL ELGORT, individually and as co-partners doing business under the firm name and style of ALLEN AND COMPANY, JACOB L. HOLTZMANN, LILLIAN HOLTZMANN, BENJAMIN H. BREWSTER, LEON COLE, L. BOYD HATCH, MAURICE L. SINDEBAND, LILLIAN SINDEBAND, HOWARD L. FOGG, RALPH B. DURELL, Executor of the Last Will and Testament of Thomas P. Durell, deceased,

Defendants,

and

HELEN S. FOGG and C. W. RETNAUER,

Defendants.

REPLY BRIEF ON BEHALF OF PETITIONER, OGDEN CORPORATION

RICHARD JOYCE SMITH,
Counsel for Petitioner.

HENRY S. REEDER,
BERNARD L. SANOFF,
Of Counsel.

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Defendants,

and

HELEN S. FOGG and C. W. RETNAUER,
Defendants.

REPLY BRIEF ON BEHALF OF PETITIONER, OGDEN CORPORATION

Respondent's brief (Point I) seeks to demonstrate that there is no conflict between the decision of the Court below and the principles laid down in the *Gully* case (299 U. S.

109). Principal reliance for this proposition is placed upon *Bell* v. *Hood,* 327 U. S. 678. This case, however, involved the question whether the Federal Court had jurisdiction of the action. That question is not now and never has been at issue in this case. Federal Court jurisdiction of the present action is conceded.

The issue here is whether a Federal Court should apply State law in a form of action to which such law was specifically directed.

Bell v. *Hood* is not controlling upon this issue, and, as we demonstrated in our principal brief, is not even apposite by way of analogy.

The essential nature of the causes of action pleaded is to enforce an accounting by corporate officers and directors for alleged breaches of their fiduciary duties. In holding that a State statute requiring the plaintiff stockholder to post security as a condition of maintaining such an action should be applied by a Federal Court, this Court in *Cohen* v. *Beneficial Industrial Loan Corporation,* 337 U. S. 541, 549-550 (1949) said:

> "The very nature of the stockholder's derivative action makes it one in the regulation of which the legislature of a state has wide powers. Whatever theory one may hold as to the nature of the corporate entity, it remains a wholly artificial creation whose internal relations between management and stockholders are dependent upon state law and may be subject to most complete and penetrating regulation, * * *. We conclude that the state has plenary power over this type of litigation."

In the *Cohen* case, jurisdiction of the Federal Court happened to be invoked upon the ground of diversity of citizenship. The issue there, however, was not whether the Federal Court had jurisdiction of the action. The issue was, as it is here, whether the Federal Court should apply

State law evincing a declared policy of regulation over the internal relation between corporate management and stockholders.

That issue should not be resolved upon the wholly artificial concept of whether the pleader may have also alleged a violation of a Federal statute such as would permit the Court to disregard as "surplusage" the allegations of diversity (R. 124).

Moreover, even if it be conceded, *arguendo,* that the plaintiffs have asserted a Federal claim which the corporation could enforce, the question still remains whether the plaintiff stockholders may enforce this claim in the corporation's behalf without regard to the substantive limitations which the State has imposed in the exercise of its "plenary power" to control derivative litigation.

It is clear that the decision of the Court below, if not in direct conflict with this Court's decision in the *Cohen* case, has placed serious and illogical limitations upon it. It was because of the *Cohen* case that the Court below frankly conceded that the correctness of its decision was "not free from doubt" (R. 127), and we submit that this very "doubt" is persuasive reason for this Court to grant certiorari.

Respectfully submitted,

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HENRY S. REEDER,
BERNARD L. SANOFF,
of Counsel.

Dated: August 31, 1950.